

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 02-0507
Sales and Use Tax
For the Years 1998-2000

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ISSUES

I. Sales and Use Tax-Exemption Certificates

Authority: IC 6-8.1-5-1 (b), IC 6-2.5-2-1, IC 6-2.5-8-8, IC 6-2.5-5-25, 45 IAC 2.2-8-8, 45 IAC 2.2-8-12, Indiana Department of Revenue Information Bulletin #10, dated February 10, 1986.

The taxpayer protests the disallowance of certain exemption certificates.

II. Sales and Use Tax-Brochures and Prizes

Authority: IC 6-2.5-3-2(a), IC 6-2.5-5-6, Maurer v. Indiana Department of State Revenue, 607 N.E.2d985 (Ind. Tax 1993).

The taxpayer protests the imposition of use tax on brochures and prizes.

III. Tax Administration-Penalty

Authority: IC 6-8.1-10-2.1, 45 IAC 15-11-2 (b)

The taxpayer protests the imposition of the ten (10%) percent negligence penalty.

STATEMENT OF FACTS

The taxpayer is an Indiana corporation operating as a wholesaler of fundraising materials such as candy and novelty items. The taxpayer's customers are typically not-for-profit organizations such as schools, youth sports leagues, and churches who use the taxpayer's services to raise money for their organizations. Occasionally there is a for-profit business as a customer. The taxpayer supplies their customers' members with brochures and selling tools for the members to show to family and friends. Orders are compiled and a total order of items is placed with the taxpayer. The taxpayer's customers pay for the orders at a wholesale price and collect the marked up price from their own customers. Therefore the not-for-profits collect and keep the difference for their fundraising efforts.

As part of the sales agreement, the taxpayer will offer to add funds to the prize accounts or they may agree to supply prizes for sales persons selling at a certain level. The taxpayer also supplies the order forms, specialty bags, and explanation letters for the fundraising members. After an audit, the Indiana Department of Revenue, hereinafter referred to as the “department,” assessed additional sales and use tax, interest, and penalty. The taxpayer protested a portion of the assessment. A hearing was held and this Letter of Findings results.

I. Sales and Use Tax-Exemption Certificates

DISCUSSION

The taxpayer protested assessments of sales tax on certain sales to two youth organizations where the exemption certificates provided by the taxpayers did not include registered retail merchant certificate numbers. The taxpayer also protested the sales tax on a third youth organization that is referred to in the audit report as having given an incomplete exemption certificate but the certificate is not currently available. The taxpayer contended that these sales qualified for a statutory exemption in that they were sales to qualified not-for-profit organizations to raise money for their exempt activities. Further, the taxpayer argued that the exemption certificates were completed in accordance with the law. The first issue to be determined is whether or not the exemption certificates were properly completed.

All tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC 6-8.1-5-1 (b).

Indiana sales of tangible personal property are subject to the Indiana sales tax unless they qualify for a statutory exemption. The sellers of the property are required to collect the sales tax from the purchasers and remit that tax to the state. IC 6-2.5-2-1.

IC 6-2.5-8-8 provides for exemption certificates from sales tax in pertinent part as follows:

- (a) A person, authorized under subsection (b), who makes a purchase in a transaction which is exempt from the state gross retail and use taxes, may issue an exemption certificate to the seller instead of paying the tax. The person shall issue the certificate on forms and in the manner prescribed by the department. A seller accepting a proper exemption certificate under this section has no duty to collect or remit the state gross retail or use tax on that purchase.
- (b) The following are the only persons authorized to issue exemption certificates:
 - (1) retail merchants, wholesalers, and manufacturers, who are registered with the department under this chapter;
 - (2) organizations which are exempt from the state gross retail tax under IC 6-2.5-5-21, IC 6-2.5-5-25, or IC 6-2.5-5-26 and which are registered with the department under this chapter; and . . .

45 IAC 2.2-8-8 clarifies the law pertaining to exemption certificates of not-for-profit organizations such as the taxpayer’s customers as follows:

- (a) Organizations exempt from gross retail tax under IC 6-2.5-5-21, IC 6-2.5-5-25, or IC 6-2.5-5-26 may register with the Not-For-Profit Section, Income tax Division, in order to issue proper exemption certificates for exempt transactions.
- (b) An exempt organization making taxable sales must register with the Central Registration Section and obtain a registered retail merchants' certificate.

45 IAC 2.2-8-12 clarifies the law concerning exemption certificates in pertinent part as follows:

- (a) Exemption certificates may be issued [sic.]only by purchasers authorized to issue such certificates by the Department of Revenue. Retail merchants, manufacturers, wholesalers and others who must register with the Department of Revenue and who qualify to purchase exempt from tax under this Act [IC 6-2.5] may issue exemption certificates with respect to exempt transactions. All persons or entities not required to register with the Department as retail merchants, manufacturers, or wholesalers, and who are exempt under this [Act IC 6-2.5]with respect to all or a portion of their purchases are authorized to issue exemption certificates with respect to exempt transaction provided an exemption number has been assigned by the Department of Revenue, or provided that the Department of Revenue has specifically provided a form and manner for issuing exemption certificates without the need for assigning an exemption number. . . .

Indiana Department of Revenue Sales Tax Information Bulletin #10 dated February 10, 1986 provides directions for the application of sales and use tax to not-for-profit corporations in pertinent part as follows:

Not-for-profit organizations (except governmental entities) are no longer required to obtain retail merchant certificates unless they conduct retail sales on which tax must be collected.

Such organizations must register with the Income Tax division of the Indiana Department of Revenue and receive a Not-For-Profit Registration Number The Not-For-Profit Registration Number may be used on sales tax exemption certificates (form ST-105) when making qualified purchases, unless the organization has been classified as a social organization and issued a number in the 800,000 series.

The law provides for two categories of organizations that can issue exemption certificates. The first is registered retail merchants. None of the three disputed exemption certificates were issued by an organization with a valid registered retail certificate number.

The second category is organizations that qualify for exemption from the payment of sales tax pursuant to certain provisions of the Indiana Code. One of those categories is not-for-profit organizations exempted at IC 6-2.5-5-25. The taxpayer contends that the exemption certificates submitted, although improperly completed, are adequate to extinguish its responsibility to collect

and remit the protested sales taxes. Since the three exemption certificates under consideration did not meet the stated standards to be valid, they cannot relieve the taxpayer of its duty to collect and remit sales taxes on items sold to these not-for-profit organizations.

Pursuant to the statute and explanatory regulation, the production of a valid exemption certificate exempts the merchant from the duty of collecting and remitting sales tax. Without a valid exemption certificate, the burden shifts back to the merchant to prove that the sales were not actually subject to sales tax as provided in 45 IAC 2.2-8-12 as follows:

(d)Unless the seller receives a properly completed exemption certificate the merchant must prove that sales tax was collected and remitted to the state or that the purchaser actually used the item for an exempt purpose. It is, therefore, very important to the seller to obtain an exemption certificate in order to avoid the necessity for such proof. . .

Although the exemption certificates presented were not adequate to exempt the taxpayer from the collecting and remitting of sales tax, the taxpayer could demonstrate that the taxpayer's customers actually used the purchased products for an exempt purpose. The taxpayer provided documentation that the soccer club and youth basketball association actually used the items for an exempt purpose.

FINDING

The taxpayer's protest is sustained as to the sales made to the soccer club and the youth basketball association. The remainder of the protest is denied.

II. Sales and Use Tax-Brochures and Prizes

DISCUSSION

Indiana imposes an excise tax on tangible personal property stored, used or consumed in Indiana when no sales tax was paid at the time of purchase unless the use qualifies for an exemption. IC 6-2.5-3-2(a).

The taxpayer purchased brochures which describe the items being sold by the fundraising customers. The brochures were included in the sales kits. The customers' members used these brochures to illustrate what they were selling to their families and friends and procure orders. The department assessed use tax on the taxpayer's use of these brochures. The taxpayer protested the assessments on the brochures based on the contention that the brochures were an integral part of the sales kit and therefore qualified for exemption pursuant to IC 6-2.5-5-6. The brochures act as both advertising for the products being sold and a means by which customers choose the products they will buy. They are clearly an essential part of the sales price. As a major cost, the cost of the brochures is factored into the cost of the candy and novelties sold and the percentage of profits going to the selling organizations. There is, however, no indication in the audit or materials provided by the taxpayer that the brochures were ever sold to the taxpayer's customers. Rather, the taxpayer provides the brochures free of charge. The taxpayer

had the option of either selling the brochures or providing them free of charge. It chose the second option. Presumably that choice offered advantages to the taxpayer. It also offered the disadvantage of subjecting the taxpayer's use of the brochures to Indiana use tax.

The taxpayer also provided prizes such as pens, radios, stuffed animals, and bicycles to serve as motivators for the customers' members making the sales. The department assessed use tax on these items. The taxpayer protested the assessment contending that the prizes were exempt from gross retail and use tax based upon the Indiana Tax Court's finding in Maurer v. Indiana Department of State Revenue, 607 N.E.2d985 (Ind. Tax 1993). That case concerned a not-for-profit organization that held a fundraising raffle for a car. The not-for-profit organization purchased a car from a dealer and then sold chances to win the car. Mr. Maurer won the raffle and was charged sales tax on the transaction transferring the car. He paid the tax and claimed a refund. The Court held that Mr. Maurer had purchased the "right to claim a prize upon the happening of a contingency." Id. at 987. Since he had not purchased tangible personal property, there was no sales tax due. Further, the Court held that the not-for-profit organization had purchased the car to be used to further its exempt not-for-profit purpose. Therefore it did not owe use tax on the use of the car.

The cited Tax Court case concerned the sale of a car to an exempt not-for-profit organization and the sale of a chance to win the car. The taxpayer's situation is different. The use tax in this instance is imposed on the taxpayer. Although the taxpayer could have chosen to do so, the taxpayer did not sell the prizes to its customers. Rather the taxpayer provided the prizes free of charge. The taxpayer was the user of the prizes. The taxpayer is like the car dealer in the cited case. Had the car dealer given the car away, the car dealer would have been liable for use tax on its use of the car.

Finding

The taxpayer's protest to the assessments of use tax on brochures and prizes is denied.

III. Tax Administration-Penalty

The taxpayer protested the imposition of the ten percent (10%) negligence penalty pursuant to IC 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2 (b) clarifies the standard for the imposition of the negligence penalty as follows:

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

During the period of the audit, the taxpayer ignored the law and departmental instructions for the payment of Indiana sales tax. The taxpayer did not pay sales tax on office supplies and computer and other equipment used in the office as clearly required by the law. This breach of the taxpayer's duty constitutes negligence.

FINDING

The taxpayer's protest is denied.

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